Review of Pooling and Unitizing

Chapter 7

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Topics

- Introduction
- Reasons for Pooling
- Pooled Units
  - Voluntary Pooling
  - Involuntary Pooling
- Pooling of Working Interests
- Federal Units
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Introduction

- Pooling, Unitization and Communitization can be defined as combining or merging of leases or other interest to erase boundary lines between leases.

- **Pooling** is the ***combining royalty interest*** in a proration unit
  - Proration unit – spacing set by governmental authority for allowable and conservation purposes

- **Unitization** are ***larger operations*** and may involve ***not only combining royalty interests but also working interest*** for the entire area

- **Communitization** is the ***pooling of federal, state or Indian*** leases into a proration unit

Reasons for Pooling

- Diversity of Ownership –
  - Pooling pulls together small tracts.
  - 40 acs oil and 640 acs gas
- Conservation
  - Regulatory agencies regulate the spacing of wells, set allowable days and promote conservation of resources. Pooling prevents unnecessary and uneconomic drilling.
- Economic considerations
  - When you combine the small tracts and are drilling fewer wells this lowers development and production costs.
- Secondary recovery & pressure maintenance operations
  - These can add large quantities to the producible reserves of a field that would not be recoverable with out unitization.

Reasons for Pooling

- What is the purpose for pooling or unitization?
  - To develop and operate a reservoir to remove the greatest amount of hydrocarbons consistent with reasonable economic practice.
  - To achieve equity among interest owners by permitting each to recover his or her fair share of the oil, gas or proceeds from it.

Pooled units

- A pooled unit is generally an area which conforms to the authorized spacing requirements and in which diverse ***royalty and/or working interests are combined***
- Created two ways:
  - **voluntary pooling** in which any parties agree to pool
  - **involuntary pooling**, or *forced* pooling, in which control is given by the state statute.

Voluntary Pooling

- Three common ways to effect voluntary pooling
  - Pooling provisions in leases
  - Pooling amendments
  - Royalty pooling agreements

Pooling Provisions

- Pooling provisions provide one or more of the following powers:
  - Option to pool all or any part of a lease
  - Operations on or production from any portion of the pooled unit.
  - Royalty is paid on the production so it is allocated without regard to location of the unit well.
  - Units may be pooled as to any one or more strata (formation).
  - Units ***do not*** have to be formed at ***any particular time***

Pooling Amendments

- When used:
  - When your lease ***does not*** contain pooling authority
- Designation of Pooled Unit (required)
  - Describes the unit area
  - States leases being committed to the unit
  - Identifies the formation or depth
  - States an effective date
  - Designates the unitized substances
- Filed in county where unit is

- Limitations:
  - Operator must dictate that pooling is necessary or advisable in order to explore or properly develop and operate the premises in compliance with spacing rules of the regulatory body or to promote conservation
  - Shape of the unit must be reasonable and must be designed so that conservation motives take precedence over lease maintenance motives

Royalty Pooling Agreements

- Formal agreements specifically drawn and designed for one proration unit.
- Signed by ***all interest owners***
- *Why use this type of agreement?*
  - not all leases contain pooling provisions
  - some owners of mineral and or royalty interests will not grant the broad pooling authority as normally contained in leases but will agree to the pooling of a specific unit for specific purposes

Involuntary pooling

- What is **involuntary pooling**?
  - small tracts or **uncommitted** *royalty and/or working interests* can be included in a proration unit of the size *authorized by the regulatory agency of the particular state*.
- Approximately 32 of the 50 states have some type of force pooling statutes.
- Very little uniformity of the provisions

Involuntary pooling provisions

- *Common provisions* in involuntary pooling:
  - What party or parties may invoke the provisions
  - Application to regulatory agency for hearing and information to be submitted in support of the application
  - Notice of the application and hearing
  - Required testimony to be presented at the hearing (by either geologist or engineer or both and testimony by a landman as to:
    - Ownership of interest
    - Response of voluntary efforts to pool
  - Matters to be set forth in the order by the regulatory agency approving the unit.

Involuntary Pooling (Texas)

- Texas Mineral Pooling Act, August 30, 1965
  - Administered by the **Railroad Commission of TX**
  - The provisions **do not** apply to reservoirs discovered and produced prior to March 8, 1961.
  - They ***cannot be invoked until after*** the RRC has established field rules for the reservoir.
  - It applies **only in situations where uncommitted interest exist in a separately owned tract** within the proration unit

Involuntary Pooling (Texas) Cont.

- Requesting party for pooling must show **a fair and reasonable offer** was to all parties to voluntarily pool
- The offer to pool and order authorizing the pooling must be **limited to productive formations** as decided by the RRC
- A **200% penalty** maybe assessed for share of the cost to force pooled WI.
- **State lands** can not be force pooled **without** the **state's consent.**

Involuntary Pooling (Oklahoma)

- Oklahoma Force Pooling Law, 1947
- States:
  - Where there are separately owned tracts or undivided interest, or both, within a spacing unit the OCC may require owners to pool and develop their lands in the spacing unit as a unit.
  - It will be under the terms and conditions that are just and reasonable and will allow the owner of the tract the opportunity to recover or receive with out unnecessary expenses

Pooling RI and WI in Oklahoma

- **Pooling Royalty Interest**
  - Request for spacing order is requested before drilling of a well – for the depths and formations where they expect to get production.
  - Pools 1/8 royalty within the spacing unit
  - Acreage is dependent on depth and the hydrocarbon being unitized
    - ***Oil Spacing –***
      - **40 acres** for oil producing less than 4,000 feet below the surface.
      - **80 acres maximum** for depths between 4,000 and 9990 feet.
      - **1150 acres is standard**
    - ***Gas Spacing –***
      - **160 acres** with 320 or 640 acres spacing

Pooling RI and WI in Oklahoma

- Pooling Working Interest
  - An area ***must be*** spaced **prior** to issuing a **force pooling order**
  - ***Non joining parties*** are given two options
    - They can put up their share of the est. drilling costs and participate
    - Or lease its interest to the drilling party for cash bonus and royalty
  - ***Leasehold interest owners***
    - Put of its share of est. drilling costs and participate
    - Sell the leasehold to the drilling party on **terms set out by the OCC**
    - **Farmout** its interest to the drilling party

Pooling of Working Interests

- Operating Agreements – An agreement between the owners of operating rights in and oil and gas property it provides for the concurrent operation of properties for the drilling and production of oil and gas.
  - Working interest can be forced pooled
  - If area greater than one proration unit – force pooling will not apply and an agreement must be made on a voluntary basis

- ***Drilling Units*** – agreements that cover a single proration unit

- ***Exploratory Units*** – agreements that cover multiple sections or proration units to share costs for wildcat exploratory units

Federal Units

- ***Three types*** of Federal Units
  - Communitization – this pooling occurs where **separate tracts under a lease cannot be independently developed** with the established spacing pattern
  - Federal Exploratory Unit – Formed prior to the drilling of the first well on the prospect. The obligation well must commence within **six months after** the approval of the unit.
    - Limited to approximately 25,000 acres from one well
    - If more acres then additional wells will need to be drilled.
    - **Participating area** – composed of lands that can reasonably be expected to be drained by the producing well
    - Operator required to file a Plan of Development with BLM for further development.
  - Secondary Recovery Unit – formed **after a field is fully developed** in order to increase the ultimate recovery by an enhanced recovery method

Federal Units – Common Features

- Unit agreements and Communitization agreements must be on forms prescribed by the Bureau of Land Management (BLM) or other federal agency
- After agreements are executed they must be approved by the BLM before it is effective
- Federal Procedures and requirements must be observed when dealing with Indian lands
- Spacing of wells is governed by the rules of the applicable state regulatory agencies
- Units are Effective on the date of the BLM approval
- State and privately owned lands are included in federal units and must agree to the inclusion of their lands and interests by ratifying the unit agreement

Fieldwide Unitization

- Field wide units (secondary units) increases the quantity of hydrocarbons produced by the injection of various substances into the formation to move additional oil into the well bore.
- Field wide units are formed by voluntary agreement or under the terms of an applicable state statute.

Fieldwide unitization or secondary recovery units

- General characteristics and features of the secondary recovery units are :
  - Unitization **applies only to the unitized formation.**
  - ***Both royalty and working interests*** are required to **consent** to the unitization.
  - **unit operator** is usually the owner of **the largest working interest** within the unit area.
  - Owners of both royalty and working interest in each individual tract within the unit area must agree to exchange their interest in a specific tract for a functional interest in total production from the entire unit.

Fieldwide unitization or secondary recovery units

- General characteristics and features of the secondary recovery units are (Cont) :
  - **Unitization** is usually **proposed after the reservoir** is essentially **fully developed** and after a pressure and/or production **decline** has been observed. The working interest owners are required to devise and adopt a plan of operation designed to increase the ultimate recovery from the unitized formation.
  - The plan of unitization **must be approved** by the applicable state regulatory agency before it can be made effective.
  - If a mutually satisfactory plan of unitization **cannot be negotiated** on a voluntary basis, one or more of the parties owning an interest in it **may invoke the provisions** of compulsory or forced pooling statues in states where these laws exist.

Compulsory Unitization Statutes

- Compulsory Unitization Statutes
  - At least 22 states have statutes providing for force pooling both WI and RI in secondary recovery units

- ***Common provisions among states***
  - Any interested party can apply for the formation of a unit
  - A notice and hearing must be held
  - All statutes require **voluntary agreement from 63-80%** of both WI and RI owners before an order to pool the remainder of the interest will be issued.

Fieldwide Units in Texas

- All fieldwide pooled units (secondary recovery units) in Texas are **voluntarily** formed under the provisions of "Agreement for Pooled Units and Cooperative Facilities in the Secondary Recovery Operations"
  - Purpose of this was to protect parties wanting to form units from prosecution under anti-trust laws
- Provisions are similar to the common provisions except:
  - RRC is only authorized to approve proposed units
  - No provision providing for compulsory unitization

Fieldwide Units in Oklahoma

- Oklahoma passed the **first comprehensive unitization statute** in the nation.
  - It provided for compulsory unitization of all oil or gas from a common source of supply
  - It follows common provisions as discussed in this chapter
  - The OCC can not force pool a unit until after **63% of the WI owners and 1/8 royalty interests** have approved the unit

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Thanks for attending!!!

Coming up:
January 31, 2013
Linda Barry
Chapter 8: Issues Affecting Ownership